



OPERATIONAL AUDITING IN HOSPITALS

Dr (Brig) AP Pandit¹ | Dr. Meenal Kulkarni² | Ms. Ishita Samanta³

¹ MD (HA) DNB (H & HA), Prof & HoD, MBA (HHM), SIHS, S B Road, PUNE-04

² MBA (HA) PhD, Asst Prof, SIHS, S B Road, PUNE-04

³ MSc. MBA (HHM), Student, SIHS, S B Road, PUNE-04

ABSTRACT

An operations audit is an examination of the operations of an ongoing business. In this audit the auditor thoroughly examines the efficiency, effectiveness and economy of the operations with which the management of the entity is achieving its objective. The operational audit goes beyond the internal controls issues since management does not achieve its objectives merely by compliance of satisfactory system of internal controls. Operational audits cover any matters which may be commercially unsound. The objective of operational audit is to examine Two E's, namely:

- **Effectiveness** – doing the right things with least wastage of resources
- **Efficiency** – performing work in least possible time

The main research question in this is to study the drawbacks in the operations. It is a future-oriented, systematic, and independent evaluation of organizational activities. The primary sources of evidence are the operational policies and achievements related to organizational objectives. Internal controls and efficiencies may be evaluated during this type of review.

An Operational Assessment Audit for a Healthcare Company usually involves studying the compliance of the operations with the company's policies and standards. The reasons behind the noncompliance are associated to their causes. The reason for lag is then studied and methods to eradicate are then thrashed out.

INTRODUCTION

In the present times companies are reshaping their strategies to achieve sustainable business growth in innovative ways, and continuing to seek value creation through improved operational performance.

Management is therefore focusing on initiatives and issues that impact upon the operating models of business activities and processes, such as operational excellence, supply chain optimization, off shoring, talent mobility, innovation, and cloud computing to name a few. Given these dynamics, internal audit is in a unique position to influence value enhancement efforts. This is achievable through Operational Auditing. Operational auditing plays an important role in today's business environment well beyond the realm of money, compliance, and traditional internal controls, and in to the realm of a trusted business partner influencing management's pursuit of operational excellence. Managers use the operational audit to evaluate and analyze the current effectiveness of a company's operations while identifying areas of potential improvement. In other words, Operational Auditing is to assist employees of the company in effectively performing their responsibilities.

OPERATIONAL AUDITING

Auditing is defined as a systematic and independent examination of data, statements, records, operations and performances (financial or otherwise) of an enterprise for a stated purpose. In any auditing the auditor perceives and recognizes the propositions before him for examination, collects evidence, evaluates the same and on this basis formulates his judgment which is communicated through his audit report.

An operational audit is a formal evaluation of the internal systems and procedures a company uses to produce goods or services. Made of at least four major steps, it tests how efficient and effective operations are, with which the management of the entity (client) is achieving its objective¹. The operational audit goes beyond the internal controls issues since management does not achieve its objectives merely by compliance of satisfactory system of internal controls. Operational audits cover any matters which may be commercially unsound. In general, the tools and processes a business uses to get a product or service to the public have to work as intended and be efficient. Businesses, therefore, use these types of audits to streamline what they are doing, with the ultimate goals being to decrease waste and boost revenue and profits.

An Operational Audit is designed to

- Understand the responsibilities and risks faced by an organization;
- Identify, with management participation, opportunities for improving control

- Provide senior management of the organization with a detailed understanding of the Operations.

DEFINITION²

According to The Institute of Internal Auditors (IIA), Operational Auditing is defined as:

"...a systematic process of evaluating an organization's effectiveness, efficiency, and economy of operations under management's control, and reporting to appropriate persons the results of the evaluation along with recommendations for improvements".

Salazar defined that Operational Auditing is a technique used by an organization to evaluate its effectiveness, efficiency, and nature of its operations and report to appropriate persons the results of the evaluation along with recommendations for improvement. The objectives are to assure management that its goals are being carried out and whether or not they are capable of being improved³.

Why Operational Audit?

Operational audit contributes to improving implementation, complying with the government organizations' procedures and providing the management with points of nonconformity so that corrective and preventive actions can be taken, thereby improving the efficiency and effectiveness of operations and increasing customers' satisfaction.

In general Operational Audit is done to answer the following four causes:

Identify poor work practices in order to improve them.

- Verify that employees implement operations in conformity with instructions and regulations, which guarantees achieving the desired effectiveness and efficiency.
- Assist in the evaluation of quality control procedures adopted in the organization.
- Evaluate implementation processes in the organization.

According to Salazar, Operational Auditing uses common sense along with logical audit techniques to apply findings to organizational objectives, operations, controls, communications, and information systems. The auditor performing the evaluation is concerned with whom, what, when, where, why, and how of running an efficient and effective operation.

This means that the auditor must have knowledge of the company's operations.

Differences between Financial Audit and Operational Audit

The most distinguishing difference between the operational audit and the traditional financial audit is the scope of the engagement. The first one includes a review of the objectives of the organization, the environment within which it operates its operating policies, personnel, and even its physical facilities.

The operational auditor will use a greater variety of audit tools to obtain evidence necessary to fulfill the objectives of the audit. The financial audit is concerned primarily with the fiscal records. Its objectives are to confirm a state of financial affairs, to verify that generally accepted accounting principles have been applied with consistency, and to express an opinion on fiscal stewardship.

Financial audit, or more accurately, an audit of financial statements, is the review of the financial statements of a company or any other legal entity, resulting in the publication of an independent opinion on whether those financial statements are relevant, accurate, complete, and fairly presented

The objective of an audit of financial statements is to enable the auditor to express an opinion whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework.

An operational audit is a more comprehensive form of an internal audit. This type of audit is attempts to improve the efficiency and the effectiveness of the internal operations.

Its objectives vary a lot and are determined by the management of the company, based on their own scope.

Operational audits may consider whether the entity:

1. Is following sound procurement practices.
2. Is acquiring the appropriate type, quality, and amount of resources when needed at the lowest cost.
3. Is properly protecting and maintaining its resources.
4. Is avoiding duplication of effort by employees and work that serves little or no purpose.
5. Is avoiding idleness and overstaffing.
6. Is using efficient operating procedures.
7. Is using the minimum amount of resources (staff, equipment, and facilities) in producing or delivering the appropriate quantity and quality of goods or services in a timely manner.
8. Is complying with requirements of laws affect the acquisition, protection, and use of the entity's resources.
9. Has an adequate system for measuring and reporting performance on economy and efficiency.

Types of Operational Audits:

Operational Audits can be divided in to three genres depending on the process of the audit and also the basis of assessment. They are

- Risk Based
- Process Oriented
- Performance Driven

Process of Operational Audit⁴

The familiarization with actual operations and operating problems is the starting point of operational audits, followed by analysis and regulations that could significantly and appraisal of the controls to assure that they are sufficient to protect the business. This, however, is only the beginning of the audit.

The auditor measures against standards in carrying out the audit. The standards

that are used in an operations audit come from two main sources. These two sources are the individual entity and the industry of which the entity is a part. Company standards that are used by operations auditors include lists of objectives, goals, plans, budgets, records of past performance, policies, procedures, and directives. Industry standards include industry averages and common business sense. True, these are not always objective standards, but they are standards none the less. There are usually five basic steps in an Operational Audit. They are:⁵

1. **Preliminary Preparation:** The auditor performs a preliminary gathering of information using various sources of information (for example, the unit's web site) to identify the possible components and concerns. It involves identifying purposes and operational areas for audit—to establish the benchmarks or standards according to which the various departments has to be assessed. The type of tool and audit to be used is also decided in this phase.
2. **Program Development:** This is done to identify the key management objectives and the key control activities performed. Identification is mainly done through interviews with the administrative staff. Questionnaires and schedules are prepared in compliance with the same. A list of departments and staff resumes are collected for the same purpose.
3. **Audit Application:** This is usually the most time consuming step in the audit and it is important for all information to be carefully recorded and documented in order to be able to refer to it after the physical audit has taken place. If the audit application step is done effectively, the reporting and follow-up step is much easier to perform.

This involved going to the various departments and getting the questionnaires filled through means of interviews. It involved sequential visiting of each ward and checking for the equipments and engineering layout of each ward. Compliance with the national and international quality standards was also checked.

4. **Market Survey / Feasibility Study** One objective of the Field Survey is to obtain confirmation of the components and major concerns of the company/ project. It involves collected primary and secondary data about the primary market in which the healthcare facility. There was also a secondary research related to the secondary market. This gave a general overview of the population and helped in changing the flow of operations or remodeling the healthcare facility as need may arise
5. **Reporting and Analyze Data and Findings:** This is perhaps the most critical part of the operational audit. The final phase of an Operational Assessment service is to provide documentation on the audit. This documentation provides a review of all of the issues found during the audit and remediation options, including recommended best practices to move forward. If a new overall solution is recommended, the details are provided in this document as well as deployment options. The reporting step should include a follow up step to determine what if any action needs to take place in order to improve the operations of the company.

It involves collecting all data and collating responses into a summary audit report. Scores are imparted to each department as per the responses filled in the questionnaire. The findings of the audit are further collated with that of the market survey/ feasibility study to come up to the most feasible option.

Comparison of Lean, Six Sigma and Operational Auditing⁶ business process, and at the same trying to reduce defects and variation using Six Sigma principles. Lean, Six Sigma and Operational Auditing can be integrated to help better assess and measure the efficiency and effectiveness of various organizational controls. Regardless of whether the organization is large or small, as an internal auditor, they are always trying to increase the effectiveness of various operational internal controls. One of the major problems in adopting Lean Six Sigma is that it could take as long as three to four months for the company to see the desired effects. Therefore, in order to keep an account of the changes of the implementation process, Operational Auditing is essential. At present times many companies are trying to implement Lean manufacturing in the System interaction not considered. Processes improved independently. Operational auditors more expert in the field of audit than in the field of business benefits⁷

Table 1: Comparison between Lean, Six Sigma and Operational Audit

PROGRAM	LEAN	SIX SIGMA	OPERATIONAL AUDITING
THEORY	Remove waste	Reduce variation	Adding value
APPLICATION GUIDELINES	1. Identify value	1. Define	1. Plan
	2. Identify value	2. Measure	2. Perform stream
	3. Flow	3. Analyze	3. Analyze
	4. Pull	4. Improve	4. Recommend
	5. Perfection	5. Control	5. Follow-up
FOCUS	Flow Focused	Problem Focused	Cross Functional Business Processes

ASSUMPTIONS	Waste removal will improve business performance. Many small improvements are better than systems analysis.	A problem exists. Figures and numbers are valued. System output improves if variation in all processes is reduced	Assessment of organization risk, capability and performance
PRIMARY EFFECTS	Reduced Flow Time	Uniform Process Output	Meeting Organizational Goals
SECONDARY EFFECTS	Uniform output. Fewer inventories. New accounting system. Flow – performance measure for managers.	Less variation. Improved quality. Less waste. Fast throughput. Fewer inventories. Fluctuation-Performance measures for managers.	Improved quality. Identify poor work Practices in order to improve them. Assist in the evaluation of quality control procedures adopted. Evaluate implementation processes. Improving the efficiency and effectiveness of operations and increasing customer satisfaction.

An operational audit has many benefits to offer. The principal benefit is that it provides departmental management with an independent answer to the question: "How well are we meeting our responsibilities?" The Operational audit provides an assessment of whether the board of directors and those who are accountable to them have fulfilled their duties, achieved their objectives, adhered to the terms of reference, and observed the limitations and restrictions imposed on them.

A further important benefit resulting from a strong operational audit program is that it will also provide an independent answer to the question: "Are there any major problems that are not being adequately dealt with?" The principal reason for undertaking this type of audit is the need for detecting and overcoming current managerial deficiencies and resulting operational problems in ongoing operations. Other benefits to management include the reassurance resulting from the knowledge that all aspects of their responsibilities are receiving unbiased independent examination and the satisfaction gained from improvements to performance resulting from action taken on issues identified by the auditor.

Some companies make planned use of operations audits for personnel development. They have a permanent operations audit manager and a nucleus of key personnel. The rest of the staff consists of people who are likely candidates for future reassignment. Staff members assigned to operations audit groups primarily to give them the exposure resulting from working in many phases of the company are moved to positions elsewhere in the company as the need arises.

Operations auditing offers potential managers the opportunities to obtain a "bird's-eye" view of the organization and the administrative process that are especially beneficial to operating personnel. Individuals with mostly hands-on experience with new problems and situations are forced by some exposure to operations auditing to make fuller use of their judgment and imagination, and so the company's manpower resource is enriched.

LIMITATIONS⁸

Like any management tool, operational audits must be understood and used properly for satisfactory results. Furthermore, they need the full backing of top management. Three of their principal constraints include time, knowledge and cost.

Time is a limitation because managers must be advised about the state of affairs in their areas of responsibility promptly enough that they can act effectively. Therefore, audits must be performed regularly and often enough so the problems can be caught before they become big or entrenched. On the other hand, audit engagements must not disrupt either productivity or morale. If they are to be performed with regularity, timeliness, and convenience, operations audits cannot be lengthy, drawn-out affairs.

Knowledge is a constraint because no one is an expert in all business fields, nor can a company afford to have on its staff a specialist on every aspect of the business that is to be audited. Necessarily, then, operational audits must be performed by individuals who are trained more fully in auditing than in what is being audited. Among other things, that means that operations audits cannot be used as a vacuum cleaner to clean up every problem; realistically, it can be used only to search for major deficiencies and opportunities for improvement. The operations auditor will not turn away from the small problems and opportunities, but discovering them will be a by-product. In any event, the auditor will detail and seek to prove only the deficiencies and opportunities for improvement that are significant in terms of dollars or effectiveness. Together, time and knowledge as constraints produce the third limitation of Cost. When the cost of a single operations audit rises above, say Rs. 100,000 or Rs. 200,000, it is likely that a good deal more than the discovery and delineation of problems or opportunities for improvement has been undertaken. As a result, auditors are often thrust into the manager's or specialist's province and, despite the greatest precautions, hostility is often stimulated.

Going beyond the above factors, the most important problem of operations auditing is that it might negatively affect a manager's morale, which could adversely affect the productivity of his area of responsibility and accountability. Utmost tact and diplomacy are required on the part of the auditor, or the operations audit will cause dysfunctional effects on those reviewed.

Overall, an audit which examines the effectiveness and efficiency, of operations

is entering a sensitive area and must be handled with a keen awareness of the human relations aspects by both the auditor and senior management. Thus, "the people problem" emerges as the most critical factor in undertaking an operations audit. In addition to making the business more efficient and profitable in the long run, an operational audit almost always provides a company with some new, fresh perspectives. It makes executives aware of problems that might not have been found otherwise and lets them evaluate risks for the future. Managers also can use results to motivate employees, as the company always has something to work towards, at the end of the process. Reviewing operational processes can be very time consuming and costly. When employees and managers are working with the auditor, they can't do other activities that might benefit the business, so projects or production might slow temporarily. Sometimes, the changes that a business makes are hard for workers to get used to, which can increase conflicts or confusion.

Hospital Operations:

Hospital Operations as defined by HIPAA can be put as:⁹

- (1) Conducting quality assessment and improvement activities, including out comes services also includes people who help patients with other needs, such as evaluation and development of clinical guidelines, provided that the obtaining of general knowledge is not the primary purpose of any studies resulting from such activities; population-based activities relating to improving health or reducing health care costs, protocol development, case management and care coordination, contacting of health care providers and patients with information about treatment alternatives; and related functions that do not include treatment;
- (2) Reviewing the competence or qualifications of health care professionals, evaluating practitioner and provider performance, health plan performance, conducting training programs in which students, trainees, or practitioners in areas of health care learn under supervision to practice or improve their skills as healthcare providers, training of non-health care professionals, accreditation, certification, licensing, or credentialing activities.
- (3) Under writing, premium rating, and other activities relating to the creation, renewal or replacement of a contract of health insurance or health benefits, and ceding, securing, or placing a contract for reinsurance of risk relating to claims for health care (including stop-loss insurance and excess of loss insurance), provided that the requirements of section 164.514(g) are met, if applicable;
- (4) Conducting or arranging for medical review, legal services, and auditing functions, including fraud and abuse detection and compliance programs;
- (5) Business planning and development, such as conducting cost-management and planning-related analyses related to managing and operating the entity, including formulary development and administration, development or improvement of methods of payment or coverage policies; and
- (6) Business management and general administrative activities of the entity, including, but not limited to,
 - (i) Management activities relating to implementation of compliance with the requirements of this sub chapter;
 - (ii) Customer service, including the provision of data analyses for policy holders, plan sponsors, or other customers, provided that protected health information is not disclosed to such policy holder, plan sponsor, or customer;
 - (iii) Resolution of internal grievances;
 - (iv) The sale, transfer, merger, or consolidation of all or part of the covered entity with another covered entity, or an entity that following such activity will become a covered entity and due diligence related to such activity.
 - (v) Consistent with the applicable requirements of section 164.514, creating de-identified health information or a limited data-set, and fund raising for the benefit of the covered entity.

Hospitals and their staff operate within an external environment shaped by gov-

ernment regulations, characteristics of their patient populations, the job market for health care professionals, and the extent of competition from other sources of care. Hospital workers also confront an internal environment shaped by leadership priorities, resources available for training and improvement initiatives, and policies regarding responses to medical errors and quality defects.

Operation Management in Hospitals

The coordination and allocation of personnel, physical space, and equipment required to meet patient needs is an important problem for hospitals. Unanticipated waits and delays add tremendous cost and can negatively impact outcomes. For this reason, policy makers advocate the study of patient flow for analyzing operational decisions. Compared to sophisticated operations management techniques used in other industries, operations management in hospitals is fairly rudimentary. Most hospitals manage their operations with census snapshot reports along with adhoc use of multiple data sources to augment their managerial intuition.

Healthcare executives and managers are always searching for better ways to improve production capacity for medical treatment and thereby, improving operational efficiency. Hospitals are faced with challenges in how to compete and remain viable in an increasingly competitive environment. Using data from a primary survey of hospitals and from various secondary sources, one can investigate the incremental effects on hospital performance of location, strategy, and technology. It is seldom found that hospital location is the hospital's choice of strategy can moderate the effect of location.

OPERATIONAL AUDITING IN HOSPITALS

Any healthcare institution can use operational auditing, or operational review, to regularly evaluate the performance of specific units or of the entire institution, to identify conditions that need the most improvement, and, thereby, to select the best cost containment and revenue-enhancing approaches. An Operational Audit for a Healthcare Company usually involves studying the departmental efficiencies and the effectiveness of their policies. The reasons behind the lag in operations are associated to their causes. The reason for lag is then studied and methods to eradicate are then thrashed out. This may lead to engineering or remodeling of the existing facility and its compounds.

METHODOLOGY

The principle and protocol followed in an Operational Audit was studied through an example of an existing healthcare model whose operations were not in compliance with its objectives or vision and through literature review. The main objectives of this Operational Audit could be summarized as follows:

- **Environment and Need Analysis** significantly related to its performance, but The first step is to perform environment and need analysis to assess if the existing strategy meets the current needs. It involves review of current business requirements for data protection and disaster recovery, taking into consideration requirements for security, compliance, and data retention.
- **Configuration Audit**
It is a comprehensive audit of the current business model. This includes an analysis of how staffs are placed, an examination of records to identify any recurring issues, a review of the equipments, operating system and current practices, and an evaluation of departmental performance. If any issues that deviate from the industrial best practices are found, course of action to resolve them are recommended.
- **Best Practices Recommendation**
If the market is found to pose a threat to the existing hospital model recommendations maybe founded to divert from the current model and best practices for the new model will be given. It acts like a way forward and is supposed to make a direct impact on the profitability of the hospital.
- **Comprehensive Documentation**
The final phase of an Operational Assessment service is to provide documentation on the audit. This documentation provides a review of all of the issues found during the audit and remediation options, including the recommended best practices to move forward. If a new overall solution is recommended, the details are provided in this document as well as deployment options. In addition to the audit details and recommendations, the needs assessment will be documented.

CONCLUSION

Operational Audit assesses the existing business model, in -terms of its operations and primary market. Auditor analyzes the current state from the health of the existing configuration, compliance to objectives, and assess whether the operations meets current business objective statements. As a result of an assessment, there is formulation of a recommended plan of action to ensure that the operations are positively affected to give better profitability. In certain cases the efficacy and effectiveness of the organization maybe hampered due to existing competition and market conditions. For negating outside influences like these and to be in a position to be able to give worthwhile suggestions a market survey is also carried forward.

To be effective, "operational auditing should be considered as an attitude, a manner of approach, analysis and thought, not as a distinct and separate type of auditing which is characterized by special programs and techniques."

Any health care institution can use operational auditing, or operational review, to regularly evaluate the performance of specific units or of the entire institution, to identify conditions that need the most improvement, and, thereby, to select the best cost containment and revenue-enhancing approaches.

REFERENCES

1. Business Dictionary, www.businessdictionary.com, accessed 14th June 2013
2. Operational Auditing: Influencing Positive Change, The Institute of Internal Auditors, 7th National Congress of Supreme Auditors, Accessed on 14th January 2014
3. Application Of An Operational Audit Model In A Not For Profit Hospital – Constantinos M. Piperis, Naval Postgraduate School, Monterey, CA, Accessed on 14th January 2014
4. Operational Auditing: Influencing Positive Change, The Institute of Internal Auditors, 7th National Congress of Supreme Auditors, Accessed on 14th January 2014
5. Operational Audit – BNP, accessed 14th June 2013
6. Lean Six Sigma and Operational Auditing as A New Paradigm for Improvement – Mohamad Reeduan Mustapha, Mohd ShaladdinMuda, The 2012 International Conference on Business and Management, 6–7 September 2012, Phuket – Thailand, Accessed on 1st February 2014
7. Application Of An Operational Audit Model In A Not For Profit Hospital – Constantinos M. Piperis, Naval Postgraduate School, Monterey, CA, Accessed on 14th January 2014
8. Section 164.501, Title 45, Code of Federal Regulations, Accessed on 6th February 2014
9. The effect of location, strategy, and operations technology on hospital performance – Susan Meyer Goldstein, Peter T. Ward, G. Keong Leong, Timothy W. Butler, Moderation Journal of Operations Management Vol 20, 2002, Accessed on 3rd February 2014.